STATE BOARD OF EQUALIZATION
STAFF LEGISLATIVE BILL ANALYSIS

Date Amended:	**5/30/01**	Bill No:	**SB 306**
Tax:	**Property**	Author:	**Poochigian**
Board Position:	**Support**	Related Bills:	**SB 933 (Ch. 352, 1999)**

BILL SUMMARY

This bill would provide that the new construction exclusion for underground storage tanks enacted into law on September 7, 1999 applies to tank work occurring prior to the effective date of that legislation on a prospective basis.

ANALYSIS

Current Law

The law generally requires that when property undergoes "new construction" the property's assessed value be increased by the value added. When the new construction involves replacing existing improvements, the value attributable to those pre-existing improvements is first deducted from the property's assessed value before adding the value for its replacement. There are some improvements that are excluded from the definition of "new construction." In these cases, while the improvements may increase the value of property, the additional value is not added to the property's assessed value and therefore the incremental value is excluded from property tax.

Revenue and Taxation Code Section 70 (e) excludes from the definition of new construction as "normal maintenance and repair[1]" the improvement, upgrade, or replacement of an underground storage tank undertaken to comply with federal, state, and local regulations on underground storage tanks. In addition, if, in the course of this work, a structure (or portion thereof) was reconstructed, the timely reconstruction of the structure is excluded from new construction as normal maintenance and repair provided the replacement structure (or portion thereof) is substantially equivalent to the prior structure in size, utility, and function. Subdivision (e) was added to the Revenue and Taxation Code in 1999 by SB 933 (Ch. 352, Poochigian).

REVISED REVENUE ESTIMATE

[1] The phrase "normal maintenance and repair" is found in Board of Equalization regulations on new construction. Property Tax Rule 463(b) (4) excludes from the definition of the new construction, "the construction or reconstruction performed **for the purpose of normal maintenance and repair**, e.g., routine annual preparation of agricultural land or interior or exterior painting, replacement of roof coverings or the addition of aluminum siding to improvements or the replacement of worn machine parts."

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the Board's formal position.

Proposed Law

This bill would add Revenue and Taxation Code Section 70.1 to provide that "For each lien date that occurs on or after January 1, 2002, an underground storage tank that, prior to September 7, 1999, was reconstructed, improved, upgraded, or replaced as described in subdivision (e) of Section 70 shall be assessed in the manner and amount as would be required if that subdivision had been operative at the time of the reconstruction, improvement, upgrading, or replacement of that underground storage tank."

In General

Property Tax System. Article XIII, §1 of the California Constitution provides that all property is taxable, at the same percentage of "fair market value," unless specifically exempted, or authorized for exemption, within the Constitution. Article XIII A, §2 of the California Constitution defines "fair market value" as the assessor's opinion of value for the 1975-76 tax bill, or, thereafter, the appraised value of property when purchased, newly constructed, or a change in ownership has occurred. This value is generally referred to as the "base year value". Barring actual physical new construction or a change in ownership, annual adjustments to the base year value are limited to 2% or the rate of inflation, whichever is less. Article XIII A, §2 provides for certain exclusions from the meaning of "change in ownership" and "newly constructed" as approved by voters via constitutional amendments.

New Construction. The constitution does not define the term "new construction." Revenue and Taxation Section 70 defines it, in part, to mean:

> Any addition to real property, whether land or improvements (including fixtures), since the last lien date.
>
> Any alteration of land or improvements (including fixtures) since the lien date that constitutes a "major rehabilitation" or that converts the property to a different use. A major rehabilitation is any rehabilitation, renovation, or modernization that converts an improvement or fixture to the substantial equivalent of a new improvement or fixture.

With respect to any new construction, the law requires the assessor to determine the added value upon completion. The value is established as the base year value for those specific improvements and is added to the property's existing base year value. When new construction replaces existing improvements, the value attributable to those preexisting improvements is deducted from the property's existing base year value. (R&T Code §71)

New Construction Exclusions. Over the years, Article XIII A, §2 of the Constitution has been amended to specifically exclude certain types of work from assessment as "new construction." Consequently, while these improvements may increase the value of the property, the additional value is excluded from taxation.

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Proposition	Election Ballot	Subject	R&T Code
8	November 1978	Reconstruction After Disaster	§70(c)
7	November 1980	Solar Energy Systems	§73
23	June 1984	Seismic Safety – Unreinforced Masonry Structures	§70(d)
31	November 1984	Fire Safety Systems	§74
110	June 1990	Disabled Accessibility Improvements – Homes	§74.3
127	November 1990	Seismic Safety - Retrofitting & Hazard Mitigation	§74.5
177	June 1994	Disabled Accessibility Improvements – All Property	§74.6
1	November 1998	Reconstruction After Environmental Contamination	§69.4

Normal Maintenance and Repair. While certain *exclusions* to the definition of "new construction" have been amended into the Constitution, the Constitution itself does not define the term "new construction." Revenue and Taxation Code Section 70 defines certain "alterations" of property to be new construction and Property Tax Rule 463 excludes such alterations from the definition of new construction when they are performed for the purpose of normal maintenance and repair. Examples noted in Rule 463 as normal maintenance and repair include the replacement of roof coverings and the replacement of worn machine parts. Prior to SB 933, the phrase "normal maintenance and repair," had not been used in statute. SB 933 specifically provided that certain underground storage tank work was to be considered "normal maintenance and repair" and therefore exempt from new construction.

Background

The following information is taken from a California Environmental Protection Agency's News Release dated December 3, 1998.

> Owners and operators of USTs across the United States had until December 22, 1998 to comply with federal and state requirements to upgrade or replace tanks and piping installed before 1984 when California's UST program and more stringent tank requirements came into effect. This deadline was initially established by the U.S. Environmental Protection Agency 10 years ago to allow tank owners sufficient time to comply with the upgrade requirements. In California, State law prohibits the

delivery of petroleum products to USTs after January 1, 1999 if those USTs have not been upgraded or replaced by the December 1998 deadline.

Local agencies regulate approximately 61,000 tanks throughout California. Of those, 55,000 are petroleum tanks and 6,000 are hazardous substance tanks. It is estimated that approximately 29,000 USTs still need to be removed, replaced or upgraded. Although most of these tanks contain petroleum products, the impact to the public will be minimal as the majority of the tanks that have yet to comply with the law are located at trucking and transportation companies, hospitals, marinas, airports, and federal, state and local agencies.

In addition to being denied gasoline delivery, owners who miss the December 22,1998 deadline will be subject to fines. If a petroleum release is discovered on the property after this deadline, owners who have not upgraded may be ineligible to receive reimbursement for cleanup costs from the State Water Resources Control Board Cleanup Fund.

Upgrades may include retrofitting an existing tank and piping with internal lining, corrosion protection, spill containment, overfill prevention equipment, striker plates and automatic pump shutdown capabilities. Replacing the tank with a new secondary tank system can also satisfy the requirement. Non-petroleum hazardous substances tank systems, like those containing waste oil or chemicals, may not be retrofitted. They must be replaced with secondary containment (double-walled) tank systems.

Upgrade work can still be done after the December 22, 1998 deadline without penalty if the tanks are emptied, temporarily closed and properly sealed prior to the deadline. Tank owners may then choose to replace, upgrade or permanently close the tanks during the temporary closure period.

COMMENTS

1. **Sponsor and Purpose.** This measure is sponsored by the author as follow up to his original underground storage tank new construction exclusion legislation (Senate Bill 933, Ch. 352, Stats. 1999). This bill is intended to ensure that on a prospective basis, tank work completed before the effective date of Senate Bill 933, which was September 7, 1999, will receive the benefit of the new construction exclusion it created.

2. **Amendments.** The May 30 amendment deletes the prior version of this bill which amended Section 70 of the Revenue and Taxation Code and instead adds a new section of law, Section 70.1. The April 3 amendment deletes the reference to Section 25299.24 of the Health and Safety Code which would have defined the terms "tank" and "underground storage tank." The definitions found in that section of code appeared to limit the underground storage tank exclusion to those holding petroleum, thereby excluding hazardous substance tanks." In addition, various associated definitions seemed to exclude certain underground storage tanks, for

example those used on farms. This definition was deleted to ensure that some tank work would not be unintentionally disqualified from receiving the exclusion.

3. **The Board of Equalization advised in its Letter to Assessors No. 99/22 and in its legislative analysis of SB 933 that the new construction exclusion created by SB 933 would apply to work completed on or after the effective date of the legislation.** Since the effective date of the legislation, September 7, 1999, was after the date that underground storage tank work must have been completed, December 22, 1998, most property taxpayers who complied timely with the tank requirements have not benefited from the exclusion. This bill specifies that the new construction exclusion applies to tank work completed before the effective date of SB 933, for tanks only, in conformity with the author's intent to protect these taxpayers from increased property taxes.

4. **This bill would not result in property tax refunds for prior tax years.** As introduced, this bill would have required refunds for prior tax years. The redrafting of this measure by the May 30 amendments is intended to preclude property tax refunds for prior tax years. The new construction exclusion would be available for tank work completed before the effective date on SB 933 on a prospective basis commencing with the January 1, 2002 lien date.

5. **This bill would not extend retroactivity to structures.** SB 933 created a new construction exclusion for both tanks and structures. With respect to structures, Section 70(e)(2) provides an exclusion for structures reconstructed as a consequence of completing work on underground storage tanks. According to the author's office, the use of the phrase "an underground storage tank" is specifically intended to limit its application to tanks. Therefore, the retroactive nature of this measure does not apply to structures (or portions thereof) that were completed prior to September 7, 1999.

6. **Administrative issues.** Information on costs related to tanks, which are classified as fixtures, is generally reported each year on the business property statement. This bill would require that previous additions to assessments for tank work be extracted and reduced to their prior levels. For tank work completed many years ago, it is possible that, in some cases, neither the assessor nor the taxpayer may still have the business property statement or other records to identify prior increases in assessments specifically related to tank work.

7. **This bill does not limit its application to tank work as of a specific commencement date.** The prior version of this bill limited its application to work undertaken after December 31, 1988, presumably the date that U.S. Environmental Protection Agency enacted its regulations to require an upgrade or replacement of tanks and piping installed before 1984. However, the new construction exclusion of Section 70 is not limited to these particular federal requirements; it applies to all "federal, state, and local regulations." Therefore, it is possible that any tank work

completed since the enactment of Proposition 13 in 1978, that otherwise qualifies, could potentially qualify.

COST ESTIMATE

The Board would incur minor absorbable costs related to informing and advising local county assessors, the public, and staff of the law changes.

REVENUE ESTIMATE (REVISED)

Background, Methodology, and Assumptions

State law and regulations required that underground storage tanks (UST's) storing petroleum and other hazardous chemicals that were installed before 1984 were to be removed, replaced or upgraded by December 22, 1998 to reduce the risk of hazardous material releases into the environment. The upgrade deadline was established by the U.S. Environmental Protection Agency in Fall 1988 and became a state requirement soon after. Since January 1, 1999, those petroleum UST's that have not been upgraded cannot be used to receive product.

Information from the counties shows that nearly all of the upgrades and replacements that will be done were completed by the deadline. The vast majority of the UST's that were installed before 1984 that were not replaced or upgraded by the deadline were removed, closed, or, in a few cases, abandoned.

Upgrading or replacing a UST required the removal of any structures, fixtures or equipment, including pumps, located above the tank. The tank would then be removed and a new tank installed or, usually in the case of an upgrade, the lining beneath the tank would be removed and a new lining installed.

The treatment of the UST upgrades as "new construction" varied from county to county. The different treatments can be categorized as follows:

1) Upgrades and replacements were treated as "new construction"

2) Upgrades and replacements were treated as normal repair and maintenance and not as "new construction.

Only the first treatment has a revenue impact under this proposal. Los Angeles County revalued the UST upgrades in 2000 under the first treatment; originally these had been valued as normal repair and maintenance. According to county estimates, this proposal would lower these assessed values by $100 million. Assuming that Los Angeles accounts for one-half of the value affected by this proposal, the estimated total assessed value added for UST upgrades amounts to $200 million statewide.

The new construction exclusion no longer applies when the service station where the tank is located changes ownership. When the service station – or its property owner –

changes ownership, the station is reassessed at its current market value. Staff estimates that, with all of the mergers, acquisitions, and other transfers in recent years, about 20 percent of the affected tanks have changed ownership.

The estimated annual revenue impact at the basic one percent property tax rate is then $200 million x 80 percent x 1 percent, or $1.6 million

Revenue Summary

The estimated annual revenue impact at the basic one percent property tax rate is $1.6 million.

Qualifying Remarks

The annual revenue impact will decrease over time as the service stations, or the property owners, change ownership and new base year values are set at full value.

Analysis prepared by:	Rose Marie Kinnee	445-6777	9/5/01
Revenue estimate by:	Aileen Takaha Lee	445-0840	
Contact:	Margaret S. Shedd	322-2376	

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